



Overview: Summary of findings and policy directions

OVERVIEW

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Introduction

This volume was prepared amidst conditions of economic uncertainty and political stress in the Arab region. The more or less broadly accepted social contract that had prevailed for decades reached its limits in the 1990s. It was followed by economic reforms that to varying degrees failed to create shared economic growth. Political reforms are now under way in many countries of the region. External factors are also in play: in addition to geopolitical considerations, the Arab region is not immune to the current turbulence in the global economy.

The region also faces the consequences of the uprisings of the Arab Spring. Since 2011, most Arab economies have been dramatically impacted by social unrest, the surge in commodity and energy prices (for oil importers), recessionary impacts affecting private and public sector sectors, increased uncertainty for investors and greater demands for expansionary expenditure for economic recovery and social justice. The unrest has already had a huge direct cost, and has also contributed to a decline in economic activity and increased unemployment. Since 2010, the decline in regional unemployment rates has been reversed, with the largest increases registered in Tunisia (about 7 percentage points), Egypt (about 3.5 percentage points) and Syria (more than 10 per cent).

All this makes the need for re-examination of the development paradigm in the Arab region even more compelling. Along with the conventional pursuit of economic growth, issues pertaining to citizens' voice and government accountability can no longer be wished away under what appeared to be the underlying philosophy of many Arab reforms in the last 20 years or so. These reforms were often captured by the phrase "economic reforms first, political reforms later". However, the delay in adopting political reforms commensurate with the rising demands of citizens

The approach "economic reforms first, political later" was neither participatory nor inclusive and proved to be unsustainable. Reforms in these two areas must now go hand in hand.

for dignity and accountability of their Governments led to the uprisings, the trajectory of which is still being shaped.

Economic growth now needs to be balanced and to create jobs and social services of the quality and quantity required to provide women and men and their families with security and dignity. On the production side, employers and the self-employed need a level playing field in order to be able to pursue legitimate profit-seeking activities, from micro and small-scale undertakings to full scale investments, and thus move away from rent-seeking activities and investments with quick financial returns that mainly benefited establishment elites and excluded the majority of ordinary citizens.

With these considerations in mind, the United Nations Development Group for Arab states/MENA in its Response Strategy & Framework for Action (2011) mandated ILO to take the lead, along with UNDP, to assess the employment situation in the Arab region and explore policy directions that would contribute to the development of a new, inclusive policy framework from a labour market perspective. This report is the outcome of this collective undertaking by the regional offices of selected specialized United Nations organizations. The aim is to improve the understanding of the underlying economic and labour market dynamics in the Arab region in order to redefine the traditional "social contract" under which the population (or, at least, part of it) exchanged political freedom in return for public sector jobs, free public services, low taxes and other state handouts.

The traditional social contract had already come under pressure by the very weight of increasing fiscal burdens on governments and rising gaps in productivity and competitiveness in the private sector. Since the 1980s, Arab countries were finding it increasingly difficult to co-opt the educated youth into relatively well-paid civil service jobs. The latter constituted a mechanism for upward social mobility and also served as a form of social protection. However, structural adjustment measures introduced in the mid-1990s reduced the ability of the State to serve this function and act as an employer of last resort. The adjustments lowered the incomes of public sector employees, privatized or reduced public expenditure on social services, while the private sector was still saddled with a weak and unaccountable system of economic governance, including non-transparent business and investment climates.

The analysis of this report encompasses these issues. It takes as a starting point that aiming for the highest possible rate of economic growth cannot ignore the quality of growth and its impact on ordinary citizens. While satisfying economic needs is always a desirable objective, policies in the Arab region must also address the demand for dignity and social justice. Employment is a key determinant of both economic and social outcomes. It has to be *decent* in the sense that it satisfies certain minimum conditions in the areas of pay and employment, social protection, social dialogue and labour standards. This would require a move away from the extractive “rentier State” to an egalitarian “productive State” based on a level playing field for all citizens, employers and workers.



Inclusive economic growth requires a move away from the extractive “rentier State” to an egalitarian “productive State” based on a level playing field for all citizens, employers and workers.

To this end, the report offers recommendations *at the regional level*, taking into consideration the diversity of the Arab region- between its three subregions that are defined in this report as follows: the Middle East (Iraq, Jordan, Lebanon, occupied Palestinian territory, Syria and Yemen), North Africa (Algeria, Egypt, Libya, Morocco, Sudan and Tunisia) and the states of the Gulf Cooperation Council (Bahrain, Kuwait, Qatar, Oman, Saudi Arabia and the United Arab Emirates).

The report aims, first, to offer policy insights to policy-makers in their twin challenge of addressing both short-term crisis effects and pre-existing structural issues; and, second, to guide regional and international organizations in their efforts to assist governments, social partners, and stakeholders in the design, implementation, monitoring and evaluation of more inclusive and better coordinated policies at national level.

Broadly speaking, priority policy areas that are more or less common in the Arab region include, at the *general* level: (a) the development and coordination of sustainable *economic* policies that would increase labour demand; (b) the introduction or improvement, where it exists, of *social dialogue*; and (c) an expansion of the coverage and improvement in the efficiency of *social protection* in order to create an effective social protection floor.

At the more *sectoral* level, this report identifies migration, active labour market policies, education and, more broadly, skills development as areas that can also make a contribution to addressing issues in the labour market. Designing and implementing such policies, as well as the more general economic ones mentioned above, would require a significant improvement in statistics and information systems in the Arab region.

The rest of this introductory chapter summarizes the main analytical findings of this report. It starts with the economic setting and subsequent reforms since the 1990s that are the main determinants of employment creation through labour demand (Chapter 1) before it examines key dimensions of labour supply such as education and labour force participation (Chapter 2). The outcomes of interaction of these two dimensions of the labour market along with social protection, affecting both the quality of employment and the level of unemployment as well as poverty and inequality, are mentioned next (Chapter 3 to 5). The report concludes with the prospects the Arab region faces and some policy directions that, if followed, can facilitate the challenging economic and political transition the region is going through (Chapter 6). Finally, the report includes two contributions from the social partners (Chapter 7 by Workers and Chapter 8 by Employers).

The labour demand side: binding macroeconomic policy constraints

This report argues that the obstacles to making productive use of the increasingly educated Arabs lie mainly on the labour demand side. The low-skill, low-productivity, low-wage economies will not be transformed into high-skill, high-productivity, high-wage economies simply by increasing and improving schools, vocational centres and universities.

A major conclusion of this report is that what constrained the creation of decent employment in the past has much to do with labour demand, the structure and nature of which was determined more by political considerations than competitive market forces. This is not surprising given the nature of the social contract and reforms that followed it, which did not create a transparent and level playing field for the private sector, a balanced public/private interface, or a distributional mechanism based on merit or need. Critical in this respect has been the role of investment, both public and private, that determines both economic growth and the way benefits are distributed.

The economic reforms downplayed the role of public investment on the assumption that it would be replaced by private investment. Private investment was expected to be more development-friendly as it would be driven by profit opportunities on the production side while meeting consumers and jobseekers' expectations on the social side. However, as this report shows, private investment failed to pick up after the reforms and continued at the traditionally low levels that had long prevailed. Foreign direct investment (FDI) in the region has been lower than in most other regions and, together with domestic investment, favoured mining and real estate, which attracted almost two thirds of the total investments between 2003 and 2010.

The economic reforms downplayed the role of public investment, introduced fiscal, trade and financial policies based more on theory than on country conditions and were overly optimistic about what the private sector could deliver.

Investment tended to favour capital bias in production. The bias in capital intensity of production, especially in countries with extractive industries, has changed somewhat in the last decade as the share of labour-intensive sectors (e.g.

construction, tourism, and trade) increased. However, these sectors remain relatively small and often attract informal arrangements that are compounded with the prevalence of casual employment in the rest of the economy. This makes many of these jobs unattractive to job-seekers.

Trade policies favoured liberalization, paying little heed to local production or their overall impact on the economy. Intra-regional exports of non-oil goods are estimated to have been around 30 per cent below their potential, while regional trading agreements have not contributed to a deeper international integration of Arab countries. Complementary investment and institutional policies, such as in the area of transport and customs clearance, if properly developed, could have eliminated a number of obstacles hampering smaller firms and increased intra-regional trade by up to ten per cent. However, trade policies were deemed to be successful based on that promotion of "trade openness" rather than the more systemic effects these policies had on the sustainability and inclusiveness of economic growth.

The sale of public assets was welcomed as a sign of an unleashing of private entrepreneurial capital, with scant attention paid to the income concentration outcomes of handing over management of public goods to private operators. Public expenditure in the Arab region has not been associated with low unemployment as it has in other regions such as East Asia, where public expenditure "crowded in" private expenditure. The efficiency of public spending was low, as large amounts of government spending were devoted to imported goods or untargeted subsidies while failing to give adequate support to the domestic economy, including manufacturing and other value-adding industries.

The privatization drive that started in Tunisia in 1988 and Egypt in 1991 was part of a wider economic reform and structural adjustment strategy often associated with expected efficiency improvements in State Owned Enterprises (SOEs), consolidation of the state budget and support to financial markets. However, for privatization to have a positive effect, the removal of *direct* political control of governments should not result in control by the establishment insiders. What is required is that private markets are genuinely competitive. In other words, the privatization process in the Arab region was not independent of political elites.

More generally, privatization is affected by factors outside the narrow microeconomic environment in which privatized firms operate. For example, successful privatization requires changes in trade, financial and foreign investment policies as well as sufficiently developed capital markets and accompanying institutional reforms. These institutional, economic and political prerequisites were largely absent in the Arab region when privatization efforts were carried out.

Financial policies, like trade policies, focused on liberalization, while high inflation rates led central bankers to focus too much on price stabilization, instead of adopting a more balanced approach including attention to productive investments and promoting full employment. While the economic reforms managed to reduce the high rates of inflation, unemployment persisted though it also started declining slowly. This suggests that structural supply bottlenecks persisted, including in the food, energy and housing markets. In some countries inflationary pressures were reinforced by political instability.

Many Arab currencies have been pegged to the US dollar and the euro. Consequently, monetary policy in the region is tied to the stance of central banks elsewhere. Any excessive interest rate spreads encourage unhealthy carry trades (speculation on currency changes), thus leaving the region's monetary authorities unarmed in the face of external pressures. Exchange rate policies can play a decisive role in a country's ability to react to external shocks, as the ongoing difficulties of the euro zone member countries currently under stress suggest. Exchange rate policies and capital controls can also affect the resource allocation between traded and non-traded sectors, hence impacting the dynamics labour demand. Adopting a more balanced approach could have created needed policy space to promote employment creation and influence the diversification of the economy.

The pace of economic diversification has been slow. Economic reforms in the Arab region were slow to develop the required improvements in the institutional and business environments. The ills of unregulated financial markets are now well recognized as a result of the 2008 global financial crisis. Producer and consumer subsidies were being eliminated, instead of being rationalized. Public investment, especially in socially beneficial infrastructure and human development, was reduced in the hope that it would be replaced by the private sector. However, privatization failed to produce the expected economic efficiency gains.

The Arab region is characterized by two distinct approaches to taxation. First, there are countries that derive revenue from oil and have little need to impose income and value added taxes. This enables oil-based economies to spend without the need to extract taxes from the population and without rigorous checks and balances. Other Arab states that do not have an energy base and have much lower per capita incomes than oil-producers depend on raising revenue through conventional taxes. To the extent that in this group of countries revenue is raised through value added taxes, it tends to be regressive and does not distribute the tax burden in relation to the size of personal income or corporate profits. A fairer taxation system can reduce inequity and have a politically stabilizing effect. For



The pace of economic diversification and structural transformation was slow, and the nexus between food insecurity, water management and rural development received little attention with adverse implications for both formal and informal employment.

example, the new government budget in Egypt envisages a capital gains tax on profits arising from stock market investment.

Despite the vast scale of food insecurity and water scarcity and the strong nexus between poverty and poor management of natural resources, economic reforms in the Arab region have displayed indifference to the environmental challenge and the deterioration of natural resources in the region. The region is marked by limited investment in the management of water resources, poor irrigation and low agricultural productivity. The ongoing population increase, though at a lower rate than before, is bound to aggravate these problems. The size and composition of population issues are also critical for the supply of labour and are discussed below.

The supply side: more education but low labour force participation

The analysis in this report points to the conclusion that jobseekers, including youth, have done what is expected of them. Their educational attainment has increased significantly along with their willingness to take up work that is available, even at existing wages. When wage employment is not available, they engage in whatever jobs they can find, including in the informal sector. Unemployment has been declining, though not uniformly across the Arab states. Understanding the dynamics of women's employment and migration policies, along with the underlying demographic changes, is key for tracing the consequences of the effects of economic reforms for employment creation.

More specifically, the labour force participation rate has not been as low as conventionally perceived. At face value, the total labour force participation rate for those aged 15 plus is only 54 per cent in the Middle East and North Africa Region (MENA) compared to a world rate of 65 per cent (excluding MENA). This substantial difference derives primarily from the position of Arab women in the labour market: the labour force participation rates for men are 76 per cent in MENA versus 74 for the rest of the world but the respective rates for women are 27 per cent versus 56 per cent.

Taking into account that the population in the Arab region is young and student enrolments have increased rapidly clarifies further the underlying dynamics of labour supply. Focusing on the working age population (15-64) and excluding students, the male labour force participation rate increases to 84 per cent in North Africa and 80 per cent in the Middle East. In fact, the labour force participation rate of working age males excluding students has increased by 4 per cent in North Africa and 6 per cent in the Middle East since 1990. Arab women's labour force participation rate also increased over time as did their educational attainment.

The labour force participation rate (excluding students) of male youth was rather similar in North Africa (68 per cent) and the Middle East (63 per cent) in 2010. These two figures were practically equal to those in 1990. In the case of female youth, the labour force participation rate (excluding students) was 32 per cent in North Africa in 2010, almost the same as it was in 1990. However, this rate for the Middle East was much lower in 2010 (only 19 per cent), although it had increased by nearly one-quarter (23 per cent) since 1990.



The aspirations of and demands for dignity by the increasingly educated job seekers, especially women, were not met because of the quality of jobs the economy was generating.

These changes in the level and gender composition of labour supply are important for assessing the labour market outcomes in the Arab region in the last couple of decades. First, compared to North Africa, the male labour force participation rate in the Middle East has room for growth (where, as mentioned, it is increasing faster, at nearly double the rate, than in North Africa). Second, and more importantly, much of the difference between these two subregions has to do with the very low female labour force participation rates in the Middle East. This implies that, in addition to economic policies addressing labour demand, employment policies in the Middle East need to pay more attention to women's issues. This proposition is reinforced in the next section, that discusses unemployment.

The differences in the labour force participation rates between North Africa and the Middle East can be compared to those of education enrolment rates. Focusing on the youth, 27 per cent of females were attending education in North Africa (5.4 million) compared to 24 per cent of males (5 million) in 2010. In the Middle East the respective numbers were lower at 21 per cent for females (1.9 million) and 22 per cent for males (2.1 million). Despite these gender differences, the increase in female education enrolments has been faster in both subregions compared to men. In the Middle East the number of female students has increased nearly six-fold since 1990 and their enrolment rate by nearly three times. Adding to these statistics, recent developments in the GCC states confirm the link between education choices and employment prospects. While in most Arab states there are typically more women attending university than men, in some GCC states women outnumber men by a ratio of 2 to 1.

As argued in this report, given labour demand constraints and institutional factors (such as regulations and norms), women are employed in the labour market only when wages are relatively high – and education is critical for that. This is also relevant in the context of a high rate of unemployment that is discussed next.

The labour market in action: mixed results across the region

Three key indicators of labour market performance are the employment/output elasticity, the employment rate and the unemployment rate. They will be examined in turn.

The employment response to output growth has been significant in the last decade across all three Arab subregions. Employment/output elasticity was 0.76 in the Middle East, 0.70 in North Africa and 0.66 in the GCC. These are high figures, not only compared to high-income, mature economies, where elasticity values close to zero are not uncommon, but also to developing countries, where they tend to be around 0.5 or even lower (for example, Asian countries have had an average elasticity value of around 0.3 during the same period). Thus, economic growth in the Arab region has not been “jobless”, although, as this report argues, any economic reform that moved countries away from the old social contract towards a greater role for the private sector was likely to increase employment.

The change in the employment rate in the Arab region following the economic reforms was commensurate to that implied by the high value of employment/output elasticity. In the last decade, the total (male and female) employment rate (excluding students) increased by 7.2 per cent in North Africa, though by only one per cent in the Middle East. The employment rate for women increased much faster than the total rate, at 22.2 per cent in North Africa and 16.1 per cent in the Middle East. These changes mask diverging changes in the employment rates for youth, however. The employment rate for male youth remained practically the same and that for female youth increased by 11.5 per cent in North Africa. However, the rate decreased for both female and male youth in the Middle East, the former by 3.6 per cent and the latter by 12.7 per cent.

These findings confirm the different labour dynamics between women and men, youth and adults and the Arab subregions and provide the background for an assessment of changes in unemployment. Unemployment in the region remains the highest of any region. However, like the labour force participation rate, the unemployment rate in the Arab region is very much influenced by the unemployment rate of women. The male unemployment rate in North Africa stands at 7.4 per cent and in the GCC at 3.1 per cent. These two rates are lower than in Central/South non-EU Europe and the Commonwealth of Independent States in Central Asia (9.8 per cent), the group of high-income countries (9.1 per cent) and sub-Saharan Africa (7.7 per cent). All Arab states in North Africa are below those rates, with the



Employment indicators for Arab men resemble those of other world regions. It is the position of women in the labour market that distinguishes the Arab region from other parts of the world.

exception of Tunisia, which has a male unemployment rate of 13.5 per cent. It is in the Middle East subregion that the male unemployment rate of 11.7 per cent remains highest in the world. What boosts the total unemployment rate in the Arab region is the female unemployment rate of 17.4 per cent. The female rates in the subregions are 24 per cent (Middle East), 16.4 per cent (North Africa) and 13.4 per cent (GCC states).

Since 1990, the unemployment rate has declined in the Arab region, but not uniformly across the subregions. It has declined most in North Africa (by 24 per cent, partly because of the large reduction of unemployment in Algeria and Morocco, followed by the GCC states (by 4.6 per cent). It has increased slightly in the Middle East (by 2.6 per cent), where the decline in the youth-to-adult population was lower and the increase in female labour force participation was higher than in North Africa. In fact, the male unemployment rate even in the Middle East has declined over time, albeit only slightly (by 0.5 per cent).

There were similar changes in youth unemployment. The youth unemployment rate declined in North Africa mainly as a result of a decline in male youth unemployment, but increased in the Middle East, mainly because of an increase in the female youth unemployment rate. However, in both cases, the youth-to-adult unemployment rate declined by around 25 per cent, a significant decrease.

It can be misleading to look at youth unemployment rates alone since the composition of the total youth population is obscured, especially where there are rising education enrolments. Examining those neither at school nor at work gives a better understanding of the situation of youth. First, the share of youth neither at school nor at work has declined significantly in the Arab region since 1990, from 50 per cent to 40 per cent of the total youth population. This decline took place across all three Arab subregions, being greatest in the Middle East and the GCC, where school enrolments increased fastest. Second, despite continuing high female youth unemployment rates, there are more male youth unemployed than women.

In conclusion, the increase in unemployment rates that followed the decline in oil prices in the early 1980s was halted and in some cases they declined in 2000s. However, changes varied according to subregion, and between youth and adults and also males and females.

Quality of employment, poverty, inequality and social protection

Few indicators can be utilized to measure the quality of employment and the relationship between employment, poverty and inequality. The reliability of these indicators can be questionable on conceptual grounds and because of the lack of good statistics in the Arab region. The measures used in this report are the share of working poor in total employment, the share of workers in vulnerable employment, differences between country-ranking based on incomes and expected human development outcomes, the wage and consumption shares in GDP, social protection measures and, finally, citizens' perceptions of their welfare prospects.

Combining the evidence on these indicators provides a generally mixed picture. The share of working poor earning \$2/day, and the share of those deemed to be in vulnerable employment, have declined in the Arab region in the last couple of decades, and declined more in the Middle East than in North Africa. However, the share of wages in GDP also fell, especially in North Africa, where it declined by 30 per cent from an already low base. Similarly, household consumption as a share of GDP declined and did so faster than in any other world region since since the mid-1990s. Although there is no available information that captures the widely believed increase in wealth inequality, income equality seems to have been stable over time. Conventional measures show that poverty is low in the Arab region and that the poverty rate has declined over time, although at a rather slow rate.

Where the Arab region seems to stand out, however, is in citizens' perception of the prospects for their standard of living. According to opinion polls, the Arab region was the only region in which citizens were more pessimistic about their prospects in 2010 than earlier in the decade. This deterioration in expectations among Arab people is particularly significant in that it applies to a period when GDP was rising, employment was increasing and unemployment was on the decline.

The situation is clearer in the area of social protection. Originally, and as part of the social contract, social protection was administered mainly through employment in the public sector and the concomitant benefits, while the majority of the population benefited – though not always equally – from various subsidies and access to expanding education and health services, which did not in most cases reach a satisfactory level. This type of approach to social protection proved fiscally unsustainable, failed to satisfy the increasing

Though employment increased and poverty was reduced, the share of wages and consumption in GDP declined faster. Citizens were more pessimistic about their prospects for their standard of living in 2010 than earlier in the decade.

aspirations of the population and in any case began to be reduced following the economic reforms. The coverage of unemployment insurance in the Arab region remained the lowest in the world till 2010, with the exception of sub-Saharan Africa, which has lower incomes and higher rates of informality than the Arab region.

The economic reforms and the receding role of the Government had implications for the management of environmental resources and their employment implications. This is especially relevant for the Arab region where agriculture remains an important employer outside the GCC economies. The scale of the food challenge in the Arab region can be inferred from the great importance governments have historically assigned to food subsidies, which have started to be reintroduced in various forms and to varying degrees since 2010. Arab low-income countries are undoubtedly the most vulnerable to food price hikes, while sustainable use of environmental resources is perhaps the most serious long-term development challenge facing the Arab region, given the higher share of food in their basket of consumption and the weak coverage of other social protection mechanisms.

Prospects

Setting the evidence contained in this report against the likely determinants of the unrest in the region, two main conclusions are, first, the economic growth rates following the post-1990s reforms were indeed high by historical standards and economic growth has not been jobless. Second, *on a per capita basis*, the increase in incomes in almost all Arab states was among the lowest in the world, and the Arab region was the one in which citizens had the least voice and in which there was the least government accountability. The Arab Spring brought to the fore the pent up aspirations of the rising and more educated middle class and increasing demands for dignity. The economic gains arising from the reforms seem to have gradually lost value in the eyes of citizens given increasing uncertainty as a result of the roll back of the State in the areas of employment, social protection and lack of transparency.

The population dynamics are likely to accentuate recent trends. The projected annual rates of growth up to 2050 are: 1.4 per cent for the total population, broken down to 0.4 per cent for children, 0.6 per cent for youth, 1.4 per cent for the working age population and 4.3 per cent for the elderly. The slowing down of the increase in the working age population and the increasing share of the elderly add to the challenges facing the Arab region.



Arab states will face future economic growth rates that fall below levels required to reduce unemployment as their populations both grow and age.

Since 2010, many Arab states have taken a double hit: lower economic growth rates and increased fiscal outlays in the form of “peace dividend”. According to the latest projections, economic growth in the Arab region up to 2015 will be among the lowest of all world regions except Latin America. North Africa is likely to have the lowest economic growth rates: 3.8 per cent compared to 4.5 for the Middle East. These rates of growth are barely adequate to reduce unemployment at any significant rate in the future.

The requirement for economic growth will not be satisfied unless macroeconomic and governance conditions improve to attract much higher rates of investment and address structural and institutional issues that were not addressed by past reforms. The post-2010 adverse effects on regional output and employment growth may take some time to subside. A particular case is that of youth, whose (relative) gains may even be reversed. The adults of the future will

be better educated than adults are now, but youth cannot go on increasing their education enrolments forever. This will make the future youth labour supply relatively less competitive compared to that of adults.

Recent evidence from crises shows that youth unemployment persists long after growth resumes. In addition, the evidence from Southern Europe in the 1970s, Latin America in the 1980s and Eastern Europe in the 1990s suggests transitions are associated with opportunities for rent seeking, untested institutional reforms and a multitude of economic challenges. Of the 103 cases of major transitions toward democracy in all regions in the past half century, almost half (46) were followed by sharp declines in per capita incomes with the cumulative difference in income growth between successful and unsuccessful reformers reaching 35 per cent in the five years following the onset of the transition.

Most governments in the Arab region adopted various labour market and social protection measures following the uprisings. These measures seem to be more reactive than the result of a vision for sustainable and shared economic and social development. They may lead to some redistribution and provide relief in the short run but could also come under the same pressures that prevailed in the past, leading to their reform or abandonment. In addition, the measures were introduced in a rather top-down manner rather than through popular representation in decision making.

The Arab countries should therefore continue with reforms, but reforms different from those introduced in the past. The findings of this report provide some guidance for policy directions to create an inclusive, more sustainable, path toward economic growth. These directions can be grouped into those that address systemic issues across the economy and those that are more specific in nature and in their objectives.

At the general level, this report recommends: (a) policy coherence that leads to better outcomes in terms of aggregate productivity gains and increases in average wages, (b) social dialogue that increases citizens’ voice and government accountability, and (c) social protection that provides income and employment security by pulling risks across the whole population, and enhances human development that would not necessarily have been possible under private insurance mechanisms. Each of these is discussed in turn below.

General policy directions

1. Macroeconomic policy coherence aimed at economic growth and shared benefits

Policies should be broadly-based and take into account their social impact. Policy-makers must bear in mind not just the theoretical effects of changing each individual policy but the combined effects of all policies in place - fiscal, monetary, financial, industrial, trade, investment, and private sector development policies. The policy package should not just aim at the fastest possible rate of economic growth but should take into account the quality of growth.

The move towards a private sector-led model needs to take into account the role of the public sector. There are important synergies between the public and private sectors. Exploring complementarities between them, through the right public/private partnerships and balance, can increase production and citizens' welfare. Where privatization is warranted, it should carry economy-wide benefits rather than constitute "denationalization" processes whose returns accrue to a small group.

The private sector should also operate in a competitive and transparent environment unlike that in the past that favoured those who were willing to strike deals with the elites and in certain economic activities only, such as those in the real estate, telecommunications, tourism, financial and banking sectors. The incentive regime should be such that private investments (including FDI) should not be associated just with quick private returns. Financial markets should be regulated to avoid the creation of asset bubbles that, in the social sector, affect adversity social insurance funds and increase the price of housing. Producer subsidies should be targeted at areas where social returns are highest. All in all, the promotion of markets should not be pursued on ideological grounds but because well-functioning markets promote both economic growth and social justice. Such an environment will avoid creating benefits only for a few through rent seeking activities. It would encourage the pursue of profits through productivity gains arising from fair competition, greater transparency and freer entry into various economic sectors. And it will apply to all entrepreneurs from the informal street vendor to foreign investors.

2. Promotion of participatory and inclusive social dialogue

Transitions entail winners and losers while inequality tends to increase during economic take-off and periods



More reforms are required but different than those of the past: Achieving productive and inclusive economic growth requires coherence between economic and social policies agreed through free and effective social dialogue.

of fast economic growth. This should be recognized but not passively accepted. Instead, governments should acknowledge the fact and devise policies to counter it and then move the economy towards a more equitable outcome. Social dialogue improves the communication between leaders and various groups of people by creating an avenue for expressing concerns and reducing misunderstandings. When disagreement remains, it provides institutionalized mechanisms for conflict resolution, for example, in determining the right balance of employment protection regulations and the socially acceptable level of wages. A stable system of labour relations would also lead to predictable outcomes and thus encourage investment, and contribute to social justice by facilitating a fairer distribution of the benefits of economic growth.

A fundamental reform of labour relations is needed in order to enable social dialogue to take place in the Arab region. The wider movement towards involving political parties, social movements and civil society organizations in the democratic process should include free and effective dialogue between employers and workers. This has been missing in the region, especially as a result of the nature of workers' organizations which, where they existed, were segmented (for example between the public and private sectors) or were co-opted by the previous regimes.

3. Expansion of coverage and increased effectiveness of social protection

Following the Arab Spring, many states in the region – and not only those affected by the uprisings – introduced, expanded or re-introduced measures to expand employment in the public sector, increased salaries and pension benefits, and so on. While understandable from a political perspective in the short run, effective and sustainable social protection requires more than just "pasting over the cracks". When properly designed and implemented, social protection serves both an investment and welfare enhancing role and has positive returns to societies. It should not be seen just as costly fiscal outlay.

The coverage of social insurance in many Arab states that is restricted to workers in the public sector and private

sector workers with regular contracts, should be extended to include all workers who can contribute to the system, including the self-employed. For those who are not able to contribute to formal social insurance schemes, social transfers can alleviate poverty or generate considerable social returns, such as well-designed cash transfers that encourage children's education and increase access to health care. Unlike in the past, food subsidies can be better designed and implemented in view of rising international prices and since economic conditions are likely to deteriorate. The necessary fiscal space can be found through better allocation and targeting of public expenditures. The region's 'demographic dividend' can be also helpful in this respect: as the share of young workers in the formal labour force increases, the ratio of beneficiaries to contributors (dependency ratio) declines.

Specific policies

The three general policies discussed are critical for setting the overall envelope for productive employment at the macro level and creating equitable societies through social protection. Both can be better achieved through inclusive representation and social dialogue. However, these policies need to be supplemented with measures that apply specifically to the labour market. These include policies for migration, active labour market programmes, and education and, more broadly, skills development. Designing and implementing these general and sectoral policies would require a significant improvement in statistics and information systems in the Arab region.

4. Improved migration management

Migration has traditionally been a feature of labour markets in the Arab region: from North Africa mainly to Europe; from the Middle East to the GCC; and more informally intra-regionally between different countries, for example from Syria to Lebanon or Egypt to Jordan. It is as much an economic issue as an issue of labour standards and human rights for *all* workers when migrants' pay and employment conditions differ from those granted to national workers. When migration policies treat migrant workers differently from nationals, they also fail to respect and protect the rights of nationals, who are asked to compete in their own country under conditions that prevail in the country of origin of migrants. Such policies lead to segmentation of the labour market, at first between national and migrant workers and then to an additional segmentation between the public sector and the private sector by the resulting preference of nationals to be employed in the public sector. This in turn creates fiscal pressures as a result of an expanding public sector, in addition to over-employment and low productivity

in the public sector that can have adverse effects on the quality of public and social services.

Migration is not just a labour market issue: it is an economic and social issue that determines the outcomes and rights of both migrants and citizens.

Migration policies should not be geared to the least labour cost option in the short-run but should contribute to the development of a high skilled/ high productivity/ high-wage economy. Otherwise, migration can accentuate inequality by giving employers access to low-wage migrants, thus increasing their profits but at the same time restricting the options for nationals and thus reducing their incomes from employment. At the level of the economy, productivity is restricted and the resulting low wages may in turn induce nationals to invest in educational fields that are less demanding. This can lead to credentialism, that is, incentives for nationals to invest in getting the minimum level or least demanding type of education that will just satisfy recruitment criteria in the public sector.

5. Well-designed employment policies and active labour market programmes

Active labour market policies (ALMPs) can help, if properly designed. These include employment services, career guidance, job counselling, labour market information, support for micro and SMEs and so on. There are many such policies and programmes in the Arab region but their targeting and implementation leave much to be desired. However, ALMPs can be useful in countering education and labour market failures, mitigating costs arising from unemployment by facilitating the reintegration in employment, and promoting efficiency and equity.

Though no substitute for the general policies mentioned earlier and the education policies mentioned below, ALMPs can help reintegrate some groups, including the youth who are in the forefront of regional developments. In this respect, promoting opportunities for youth entrepreneurship can boost economic growth and create jobs for young people. Related to this are necessary improvements in the regulatory environment that would make it easier for businesses, especially small and micro-enterprises – including those in the informal economy – to operate and grow.

6. Increased quality and greater relevance of education and training

Despite impressive recent gains, there is still room for improvement in access to, quality and relevance of education. Access remains limited, especially for girls in some countries, such as Morocco, Yemen and the sub-Saharan Arab states. Recent comparative analyses of learning outcomes of students confirm that average scores in all participating Arab countries are below the international average. Analysis of these results further reveals that the share of inequality in test scores accounted for by family background and community characteristics (inequality of opportunity) is high in several countries including Egypt, Lebanon and Tunisia where inequality is comparable to that in some Latin American countries, which are generally considered more unequal than Arab countries.

Education could also be more relevant to the needs of the labour market, especially the private sector. Curricula should be geared to the demands of the modern private sector. They should change accordingly as conditions in the private sector change and, if they cannot anticipate future changes, they should also offer opportunities for lifelong learning. Linking training to the needs of the labour market can be best served and augmented by involving employers in design and implementation as well as funding as such training will be valued by employers.

Though education output may not have been a constraint to the employability of job seekers so far, it can become so in the future. Improvements in quality and relevance of education are necessary and feasible.

More and better education, combined with still relatively high shares of youth in the population, can result in a “demographic dividend”. Though there are no estimates of the effect of a high share of young and more educated workers in the Arab region, this favourable change in the composition of the labour force has been estimated to have contributed about one third of the increase in East Asian per capita GDP growth between 1965 and 1990, and that was a period of very high economic growth in East Asia.

7. Better statistics and effective monitoring and evaluation of policies and programmes

Data limitations, in terms of availability and quality, impose a significant constraint on economic analysis and policy design in the Arab economies. In addition, the relative absence of statistics makes it difficult to monitor and evaluate policies and programmes and can produce misleading results. The statistical challenge is even more important during periods of rapid change, especially adverse change, such as crises.

The absence of good statistics on salaries and wages constitutes another shortcoming in the region and perhaps one of the most important ones. There is very little regional information on wage levels and the composition of labour earnings, let alone changes in them over time.

Another area in which data are lacking relates to under-employment. In fact, the official measurement of unemployment may be meaningless when informal activities or inactivity have sizeable proportions. Only a few countries have incorporated informal employment modules in their labour force and establishment surveys. Others have conducted informal economy surveys though sporadically or only recently. If the structure and flows in and out of the informal sector are unknown, policymakers may miss a large part of ordinary citizens’ employment effort and the changes in the labour market.

There are also other statistical areas that need additional attention. One such is “follow-up” surveys, as it is important to establish baselines for tracing changes over time. These surveys can be cross-sectional with retrospective questions or, ideally, panel/longitudinal. The region has a nearly complete lack of the latter type of survey.